

Legislative Audit Division

State of Montana



Report to the Legislature

November 1996

Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 1996

State Auditor's Office

This report contains three recommendations to the office related to:

- ▶ Expenditure abatements.
- ▶ General Fund transfers.
- ▶ Reinsurance Board legislation.

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FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Legislative Audit Division to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act of 1984 and Amendments of 1996, and OMB Circular A-128 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 1995 has been issued. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone: (406) 444-3616

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Helena MT 59620-1705
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LEGISLATIVE AUDIT DIVISION

November 1996

To the Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the State Auditor's Office for the two fiscal years ended June 30, 1996. Included in this report are three recommendations concerning expenditure abatements, General Fund transfers, and legislation to clarify the status of the Reinsurance Board. The office's written response to the audit recommendations is included in the back of the audit report.

We thank the State Auditor and his staff for their assistance and cooperation.

Sincerely,

A handwritten signature in black ink, appearing to read "Scott A. Seacat", with a long horizontal flourish extending to the right.

Scott A. Seacat
Legislative Auditor



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Legislative Audit Division

Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 1996

State Auditor's Office

Members of the audit staff involved in this audit were Brenda Bokovoy, Cindy S. Jorgenson, Jim Manning, and Emlyn Neuman-Javornik.

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Elected and Administrative Officials

| | | |
|-------------------------------|---------------|---|
| State Auditor's Office | Mark O'Keefe | State Auditor |
| | Rusty Harper | Deputy State Auditor |
| | Frank Cote | Deputy Insurance Commissioner |
| | Renee Erdmann | Acting Deputy Securities Commissioner |
| | John Huth | Administrator Central Administration |

State Auditor's Office

This audit report is the result of our financial-compliance audit of the State Auditor's Office for the two fiscal years ended June 30, 1996. The report contains three recommendations where the office could enhance compliance with state laws and policies.

The first recommendation addresses the improper abatement of insurance and securities examination expenditures. The report discusses understatements of amounts spent caused by a conflict between the language of the appropriation bill, which directs the office to abate the expenditures, and state law, which requires the accounting records of the state to be in accordance with generally accepted accounting principles.

The second recommendation discusses the need to develop procedures to ensure excess revenue in the Special Revenue Fund is transferred to the General Fund as required by state law. The office could enhance compliance with the law by establishing formal policies to monitor the Special Revenue Fund fund balance and make transfers on a timely basis.

The third recommendation discusses the need for legislation to clarify the legal status of the Reinsurance Board which administers the Montana Small Employer Health Reinsurance Program. This issue was a prior recommendation. In our prior audit report we noted there is a conflict in the state laws regarding whether this program is a state program, to be administered as a state agency, or a nonprofit, nonstate entity.

Office management concurred with all recommendations.

Report Summary

The listing below serves as a means of summarizing the recommendations contained in the report, the office's response thereto, and a reference to the supporting comments.

Recommendation #1 We recommend the State Auditor's Office develop appropriate methods to ensure the financial activity related to examinations of insurance and securities companies are properly recorded on the state's accounting records. 6

State Auditor's Response: Concur. See page B-3.

Recommendation #2 We recommend the State Auditor's Office develop formal procedures to ensure portfolio registration fee revenue is transferred to the General Fund in a timely manner. 7

State Auditor's Response: Concur. See page B-3.

Recommendation #3 We recommend the State Auditor's Office seek legislation to clarify whether the Reinsurance Board is a state program or a nonprofit, nonstate entity. 9

State Auditor's Response: Concur. See page B-4.

Introduction

General

We performed a financial-compliance audit of the State Auditor's Office for fiscal years 1994-95 and 1995-96. The objectives of our audit were to:

1. Determine if the office complied with applicable laws and regulations.
2. Make recommendations for improvement in the administrative and accounting controls of the office.
3. Determine if the office's financial schedules present fairly the results of operations for the two fiscal years ended June 30, 1996.
4. Determine the implementation status of prior audit recommendations.

This report contains three recommendations to the office. Other areas of concern deemed not to have a significant impact on the successful operations of the programs within the State Auditor's Office are not specifically included in the report, but have been discussed with management.

In accordance with section 5-13-307, MCA, we analyzed and disclosed the cost, if significant, of implementing the recommendations.

Office Background and Organization

The State Auditor's Office (office) was established by Article VI, Section 1 of the Montana Constitution. The State Auditor is both the ex-officio Commissioner of Insurance and the ex-officio Commissioner of Securities. The State Auditor licenses and regulates insurance companies and agents within the state, and regulates and registers securities dealers.

The office is organized as follows:

1. The Central Administration Division is responsible for the administrative, budgeting, personnel, and accounting functions of the office.

Introduction

2. The Insurance Division regulates the insurance industry in Montana. Its duties include: resolving insurance consumer inquiries and complaints involving agents, coverage, and companies; licensing and reviewing the market and financial condition of insurance companies; collecting the insurance premium tax; reviewing all rates and forms used by insurance companies; licensing, testing, and administering a continuing education program for all agents seeking to conduct insurance business in the state; and investigating insurance code and rule violations.
3. The Securities Division is responsible for the administration and enforcement of the Securities Act of Montana. The division is responsible for the registration of securities issuers, salespeople, investment advisers, broker-dealers, and investment adviser representatives. Additionally, it investigates instances of unregistered or fraudulent securities transactions.

The office is responsible for distributing a portion of insurance premium taxes to the Montana Public Employees' Retirement Division and to fire and police departments in qualifying Montana cities and towns. The office also distributes federal forest reserve moneys to Montana counties.

Effective July 1, 1995, responsibility for the state warrant writing system and bad debt collection function was transferred to the Department of Administration.

Prior Audit Recommendations

Prior Audit Recommendations

We performed the prior financial-compliance audit of the office for the two fiscal years ended June 30, 1994. The report contained seven recommendations to the office. During the current audit, we determined the office implemented six of the seven recommendations. The recommendation not implemented deals with legislation regarding the Reinsurance Board and is discussed on page 7.

Findings and Recommendations

State Compliance

We reviewed state laws pertaining to the office. The following sections discuss instances where the office could enhance compliance with laws and state policies or clarify issues noted during the audit.

Abatement of Examination Expenditures (Off Budget vs. Off Book)

State law requires the State Auditor's Office to conduct examinations of insurance companies and securities companies doing business in the state. In our financial-compliance audit for the two fiscal years ended June 30, 1992, we determined that expenses related to these examinations were not recorded on the state's accounting records. The office corrected the problem and properly recorded these expenditures through fiscal 1994-95. However in fiscal 1995-96, the office abated these expenditures because of language contained in The General Appropriations Act of 1995 (House Bill 2). The appropriation act states, "The state auditor shall charge companies directly for examinations and abate expenditures."

The appropriation bill language conflicts with section 17-1-102 (2), MCA, and state accounting policy (Management Memo 2-94-2). State law requires the accounting records of the state will show the receipt, use, and disposition of all funds in accordance with generally accepted accounting principles. The Attorney General stated in Volume 39, Number 25, Opinions of the Attorney General, that "Appropriation bills should not be held to amend substantive statutes by implication."

Determining whether this activity should be budgeted (requiring an appropriation) or nonbudgeted is a budgetary policy decision for the legislature. However, the question of this activity being recorded on the state's accounting records is a matter of state law and generally accepted accounting principles. By abating expenditures the office is understating the costs associated with the insurance and securities programs on the states accounting records (SBAS). The abatement of expenditures also understates revenues collected from the companies. The money received from the insurance companies should be recorded as revenue.

We determined the office improperly abated expenditures of approximately \$98,165 in the two programs during fiscal 1995-96.

Findings and Recommendations

The abatements by program were \$90,815 in the insurance program and \$7,350 in the securities program. In order to comply with state law and policy, the office should record all costs associated with the examination of insurance and securities companies as expenditures and all reimbursements received as revenue.

Office officials stated they were unsure who initially proposed the idea to abate expenditures, but said it came up in discussions during the appropriations hearings in the last legislative session.

Recommendation #1

We recommend the State Auditor's Office develop appropriate methods to ensure the financial activity related to examinations of insurance and securities companies are properly recorded on the state's accounting records.

Transfers to the General Fund

Portfolio registration fees are fees collected from the registration of securities offered for sale in the state. Section 30-10-115, MCA, requires the office to transfer any excess revenues from the portfolio registration fees to the General Fund. We noted the office could enhance compliance with the law by developing formal procedures for monitoring and making transfers to the General Fund. The following schedule reflects the activity and transfers for the portfolio registration program since its inception in fiscal 1993-94.

| Fiscal Year | Excess Revenues over Expenditures | Transferred to General Fund | Number of transfers | Ending Fund Balance |
|-------------|-----------------------------------|-----------------------------|---------------------|--------------------------|
| 1993-94 | \$1,024,735 | \$1,220,400 | two | (\$135,599) ¹ |
| 1994-95 | \$1,333,828 | \$420,000 | one | \$912,828 |
| 1995-96 | \$1,527,544 | \$1,911,627 | two | \$527,545 |

¹ Transfer amount was not calculated correctly, resulting in too much being transferred, resulting in the negative fund balance.

Findings and Recommendations

Office personnel stated they do not monitor the portfolio fee activity on a regular basis, but have an informal system to monitor the activity and make a transfer approximately twice a year. They do not transfer all of the fund balance at one time because the revenue is cyclical. Most of the fees are collected during the fall months.

The office's budgeted expenditures from these fees were \$80,228 for fiscal 1993-94, \$64,411 for fiscal 1994-95 and \$83,096 for fiscal 1995-96. The fiscal year 1994-95 and 1995-96 ending fund balances greatly exceed amounts necessary to fund the operations for the succeeding year. Failure to properly transfer the excess revenue understated the state General Fund balance by approximately \$829,621 and \$441,904 at June 30, 1995 and 1996, respectively.

Based on the excess of revenues over expenditures and the fund balances noted above, the office could improve compliance with the law by increasing the General Fund transfer and making it more timely. The office could accomplish this by comparing the level of expenditures with the amount and timing of the fee revenue. After the majority of the fees are collected in the fall, the fund balance should approximate the remaining unexpended appropriation balance for the current fiscal year. By comparing expenditure activity to the revenue cycle the office could develop a plan to retain fees sufficient to meet the immediate operating needs of the program.

Recommendation #2

We recommend the State Auditor's Office develop formal procedures to ensure portfolio registration fee revenue is transferred to the General Fund in a timely manner.

Reinsurance Board Legislation

Our prior audit discussed the Reinsurance Board created under section 33-22-1818, MCA. We noted there is a conflict in the state laws regarding the Montana Small Employer Health Reinsurance Program administered by the Board. We recommended that legislation be enacted to clarify whether this is a state program, to be administered as a state agency, or a nonprofit, nonstate entity.

Findings and Recommendations

Office officials concurred with the recommendation, stating the Board should be a nonprofit, nonstate entity. They also stated they would seek legislation to clarify this position. However, officials stated during the current audit they thought they had gained clarification through the budgeting process. The majority of the activity is “off-book” which they believe makes the reinsurance board a “non-state” entity.

The conflict in the law arises in the language regarding the selection of the Board. The Board consists of nine members appointed by the State Auditor plus the commissioner or his designated representative who shall serve as an ex officio member of the Board. A vacancy on the Board must be filled by the commissioner and the commissioner may remove a board member for cause. The Board must submit a plan of operations to the commissioner subject to his approval. This language indicates the Board is under the direct control of the commissioner and should be considered a state agency. Under these circumstances, where the Board is under the direct control of the commissioner, generally accepted accounting principles require that the financial activity of the Board be included and reported in the accounting records for the office.

However, section 33-22-1818, MCA, provides in part:

“(1)There is a nonprofit entity to be known as the Montana small employer health reinsurance program.”

The legislature did not denominate the program as a state program or state agency, but rather a “nonprofit entity.”

Section 33-22-1819, MCA, provides in part:

“(4)The program has the general powers and authority granted under the laws of this state to insurance companies and health maintenance organizations . . .

(11)The program is exempt from taxation.”

By giving the program the general powers and duties of an insurance company the legislature is treating the program as a private

Findings and Recommendations

insurance carrier. The fact the legislature exempted the program from taxation indicates the legislature believed the program could be taxed as a private insurance carrier without the exemption. These factors indicate the program should be considered a “nonstate” entity.

Because the office did not implement the prior recommendation, we repeat it in this report.

Recommendation #3

We recommend the State Auditor’s Office seek legislation to clarify whether the Reinsurance Board is a state program or a nonprofit, nonstate entity.

Independent Auditor's Report & Agency Financial Schedules

MONTANA LEGISLATIVE BRANCH

Legislative Auditor
Scott A. Seacat

Legal Counsel:
John Northey



Deputy Legislative Auditors:
Mary Bryson
Operations and EDP Audit
James Gillett
Financial-Compliance Audit
Jim Pellegrini
Performance Audit

LEGISLATIVE AUDIT DIVISION

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying financial schedules of the State Auditor's Office for each of the two fiscal years ended June 30, 1995 and 1996, as shown on pages A-5 through A-19. The information contained in these financial schedules is the responsibility of the office's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosure in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1, the financial schedules are presented on a comprehensive basis of accounting other than generally accepted accounting principles. The schedules are not intended to be a complete presentation and disclosure of the office's assets, liabilities, and cashflows.

In our opinion, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances of the State Auditor's Office for the two fiscal years ended June 30, 1995 and 1996, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

A handwritten signature in black ink that reads "James Gillett".

James Gillett, CPA
Deputy Legislative Auditor

August 8, 1996

STATE AUDITOR'S OFFICE
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1996

| | General Fund | Special Revenue Funds | Internal Service Funds | Agency Funds | Expendable Trust Funds ² |
|--|-------------------|-----------------------------|------------------------------|-------------------------|---|
| FUND BALANCE: July 1, 1994 | \$ 0 | \$ 511,464 | \$ 49,220 | | \$ 0 |
| PROPERTY HELD IN TRUST: July 1, 1994 | | | | \$ 174,495 | |
| ADDITIONS: | | | | | |
| Fiscal Year 1994-95 | | | | | |
| Budgeted Revenues & Transfers In | 27,741,462 | 25,626,108 | 135,602 | | |
| Nonbudgeted Revenues & Transfers In | | | | | 225,826 |
| Prior Year Revenue Adjustments | | 3,500 | | | |
| Prior Year Expenditure Adjustments | 3,488 | 3,447 | 315 | | |
| Direct Entries to Fund Balance | 2,535 | | | | 187,055 |
| Additions to Property Held in Trust | | | | 3,184,612 ¹ | |
| Fiscal Year 1995-96 | | | | | |
| Budgeted Revenues & Transfers In | 29,595,069 | 11,902,952 | | | |
| Prior Year Revenue Adjustments | | 4,856 | | | |
| Direct Entries to Fund Balance | 1,911,627 | | 7,852 | | |
| Additions to Property Held in Trust | | | | 10,678,593 ¹ | |
| Total Additions | <u>59,254,181</u> | <u>37,540,863</u> | <u>143,769</u> | <u>13,863,205</u> | <u>412,881</u> |
| REDUCTIONS | | | | | |
| Fiscal Year 1994-95 | | | | | |
| Budgeted Expenditures & Transfers Out | 2,083,443 | 25,193,754 | 191,336 | | |
| Support to State of Montana | 24,393,151 | | | | |
| Nonbudgeted Expenditures & Transfers Out | | | 1,653 | | 211,976 |
| Cash Transfers Out | | 75,254 | | | |
| Direct Entries to Fund Balance | | 284,400 | | | |
| Prior Year Revenue Adjustments | 1,270,891 | | | | |
| Reductions to Property Held in Trust | | | | 3,251,840 ¹ | |
| Fiscal Year 1995-96 | | | | | |
| Budgeted Expenditures & Transfers Out | 2,093,038 | 10,437,242 | | | |
| Support to State of Montana | 29,253,574 | | | | |
| Nonbudgeted Expenditures & Transfers Out | | 34,282 | | | |
| Prior Year Expenditure Adjustments | 2,349 | | | | |
| Cash Transfers Out | | 1,307 | | | |
| Direct Entries to Fund Balance | | 1,911,627 | | | 200,905 |
| Prior Year Revenue Adjustments | 157,735 | | | | |
| Reductions to Property Held in Trust | | | | 10,785,860 | |
| Total Reductions | <u>59,254,181</u> | <u>37,937,866</u> | <u>192,989</u> | <u>14,037,700</u> | <u>412,881</u> |
| FUND BALANCE: June 30, 1996 | \$ 0 | \$ 114,461 | \$ 0 | | \$ 0 |
| PROPERTY HELD IN TRUST: June 30, 1996 | | | | \$ 0 | |

¹ See note 8 on page A-19.

² See note 5 on page A-18.

This schedule is prepared from the Statewide Budgeting & Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-15.

STATE AUDITOR'S OFFICE
SCHEDULE OF TOTAL REVENUES, TRANSFERS IN & OTHER ADDITIONS
FOR THE FISCAL YEAR ENDED JUNE 30, 1996

| | General Fund | Special Revenue Funds | Total |
|--|-------------------|-----------------------------|------------------------|
| TOTAL REVENUES BY CLASS | | | |
| Licenses & Permits | \$ 6,199,826 | \$ 2,062,662 | \$ 8,262,488 |
| Taxes | 23,118,835 | 9,808,124 | 32,926,959 |
| Investment Earnings | | | |
| Fines & Forfeits | 118,673 | 2,022 | 120,695 |
| Grants, Contracts & Donations | | 35,000 | 35,000 |
| Federal ¹ | | | |
| Total Revenues | <u>29,437,334</u> | <u>11,907,809</u> | <u>41,345,142</u> |
| Less: Nonbudgeted Revenues | (1) | 1 | 0 |
| Prior-Year Revenue Adjustments | <u>(157,735)</u> | <u>4,856</u> | <u>(152,879)</u> |
| Actual Budgeted Revenues | 29,595,069 | 11,902,952 | 41,498,021 |
| Estimated Revenues | 29,558,729 | 26,494,745 | 56,053,474 |
| Budgeted Revenues Over(Under) Estimated | <u>\$ 36,340</u> | <u>\$ (14,591,793)</u> | <u>\$ (14,555,453)</u> |
| BUDGETED REVENUES OVER(UNDER) ESTIMATED BY CLASS | | | |
| Licenses & Permits | \$ 818,742 | \$ 61,060 | \$ 879,802 |
| Taxes | (846,074) | 125 | (845,949) |
| Investment Earnings | | (150,000) | (150,000) |
| Fines & Forfeits | 63,672 | (2,978) | 60,694 |
| Federal ¹ | | (14,500,000) | (14,500,000) |
| Budgeted Revenues Over(Under) Estimated | <u>\$ 36,340</u> | <u>\$ (14,591,793)</u> | <u>\$ (14,555,453)</u> |

¹ See note 7 on page A-19.

This schedule is prepared from the Statewide Budgeting & Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-15.

STATE AUDITOR'S OFFICE
SCHEDULE OF TOTAL REVENUES, TRANSFERS IN & OTHER ADDITIONS
FOR THE FISCAL YEAR ENDED JUNE 30, 1995

| | General Fund | Special Revenue Funds | Internal Service Funds ¹ | Expendable Trust Funds ¹ | Total |
|--|---------------------|-----------------------------|---|---|---------------------|
| TOTAL REVENUES BY CLASS | | | | | |
| Licenses & Permits | \$ 5,857,412 | \$ 1,940,121 | | | \$ 7,797,533 |
| Taxes | 20,570,691 | 8,523,659 | | | 29,094,350 |
| Charges for Services | | 521,524 | \$ 135,602 | | 657,126 |
| Investment Earnings | | 149,437 | | | 149,437 |
| Fines & Forfeits | 42,468 | 12,586 | | | 55,054 |
| Grants, Contracts & Donations | | | | \$ 225,826 | 225,826 |
| Federal | | 14,482,281 ² | | | 14,482,281 |
| Total Revenues | <u>26,470,571</u> | <u>25,629,608</u> | <u>135,602</u> | <u>225,826</u> | <u>52,461,607</u> |
| Less: Nonbudgeted Revenues | | | (0) | 225,826 | 225,826 |
| Prior-Year Revenue Adjustments | <u>(1,270,891)</u> | <u>3,500</u> | | | <u>(1,267,391)</u> |
| Actual Budgeted Revenues | <u>27,741,462</u> | <u>25,626,108</u> | <u>135,602</u> | | <u>53,503,172</u> |
| Estimated Revenues | <u>25,306,500</u> | <u>24,730,896</u> | <u>197,205</u> | | <u>50,234,601</u> |
| Budgeted Revenues Over(Under) Estimated | <u>\$ 2,434,962</u> | <u>\$ 895,212</u> | <u>\$ (61,603)</u> | <u>\$ 0</u> | <u>\$ 3,268,571</u> |
| BUDGETED REVENUES OVER(UNDER) ESTIMATED BY CLASS | | | | | |
| Licenses & Permits | \$ 894,240 | \$ 430,398 | | | \$ 1,324,638 |
| Taxes | 1,553,254 | (45,967) | | | 1,507,287 |
| Charges for Services | | (13,522) | \$ (61,603) | | (75,125) |
| Investment Earnings | | 39,436 | | | 39,436 |
| Fines & Forfeits | (12,532) | 2,586 | | | (9,946) |
| Federal | | 482,281 | | | 482,281 |
| Budgeted Revenues Over(Under) Estimated | <u>\$ 2,434,962</u> | <u>\$ 895,212</u> | <u>\$ (61,603)</u> | | <u>\$ 3,268,571</u> |

¹ See note 5 on page A-18.

² See note 7 on page A-19.

This schedule is prepared from the Statewide Budgeting & Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-15.

STATE AUDITOR'S OFFICE
SCHEDULE OF TOTAL EXPENDITURES, TRANSFERS OUT, & OTHER REDUCTIONS BY OBJECT BY PROGRAM
FOR THE FISCAL YEAR ENDED JUNE 30, 1996

| | Central Management | Insurance | Securities | Local Assistance Distributions ¹ | Pension Adj Retired Firemen ¹ | Total |
|------------------------------------|-----------------------|---------------------|-------------------|---|--|----------------------|
| PROGRAM EXPENDITURES BY OBJECT | | | | | | |
| Personal Services | | | | | | |
| Salaries | \$ 215,967 | \$ 1,097,822 | \$ 254,351 | | | \$ 1,568,140 |
| Employee Benefits | 53,927 | 274,840 | 64,127 | | | 392,894 |
| Total | <u>269,894</u> | <u>1,372,662</u> | <u>318,478</u> | | | <u>1,961,034</u> |
| Operating Expenses | | | | | | |
| Services | 14,824 | 145,499 | 27,618 | | | 187,941 |
| Supplies & Materials | 14,344 | 66,281 | 13,444 | | | 94,069 |
| Communications | 7,870 | 130,395 | 19,198 | | | 157,463 |
| Travel | 1,168 | 36,333 | 9,701 | | | 47,202 |
| Rent | 9,747 | 39,614 | 10,993 | | | 60,354 |
| Repair & Maintenance | 2,182 | 4,813 | 1,191 | | | 8,186 |
| Other Expenses | 617 | 39,956 | 4,924 | | | 45,497 |
| Total | <u>50,752</u> | <u>462,891</u> | <u>87,069</u> | | | <u>600,712</u> |
| Equipment and Intangible Assets | | | | | | |
| Equipment | | 30,104 | 28,926 | | | 59,030 |
| Total | | <u>30,104</u> | <u>28,926</u> | | | <u>59,030</u> |
| Local Assistance | | | | | | |
| From Federal Sources | | | | | | |
| From Other Income Sources | | | | \$ 8,895,849 | \$ 1,050,286 | 9,946,135 |
| Total | | | | <u>8,895,849</u> | <u>1,050,286</u> | <u>9,946,135</u> |
| Total Program Expenditures | <u>\$ 320,646</u> | <u>\$ 1,865,657</u> | <u>\$ 434,473</u> | <u>\$ 8,895,849</u> | <u>\$ 1,050,286</u> | <u>\$ 12,566,911</u> |
| PROGRAM EXPENDITURES BY FUND | | | | | | |
| General Fund | \$ 296,395 | \$ 1,437,970 | \$ 361,021 | | | \$ 2,095,386 |
| Special Revenue Fund | 24,251 | 427,687 | 73,452 | \$ 8,895,849 | 1,050,286 | 10,471,525 |
| Total Program Expenditures | <u>320,646</u> | <u>1,865,657</u> | <u>434,473</u> | <u>8,895,849</u> | <u>1,050,286</u> | <u>12,566,911</u> |
| Less: Nonbudgeted Expenditures | | 34,282 | | | | 34,282 |
| Prior-Year Expenditure Adjustments | | 2,535 | (186) | | | 2,349 |
| Budgeted Expenditures | <u>320,646</u> | <u>1,828,840</u> | <u>434,659</u> | <u>8,895,849</u> | <u>1,050,286</u> | <u>12,530,280</u> |
| Actual Budget Authority | 324,494 | 1,871,573 | 439,840 | 8,896,000 | 1,150,000 | 12,681,907 |
| Unspent Budget Authority | <u>\$ 3,848</u> | <u>\$ 42,733</u> | <u>\$ 5,181</u> | <u>\$ 151</u> | <u>\$ 99,714</u> | <u>\$ 151,627</u> |
| UNSPENT BUDGET AUTHORITY BY FUND | | | | | | |
| General Fund | \$ 3,848 | \$ 42,623 | \$ 5,070 | | | \$ 51,541 |
| Special Revenue Fund | | 110 | 111 | \$ 151 | 99,714 | 100,086 |
| Unspent Budget Authority | <u>\$ 3,848</u> | <u>\$ 42,733</u> | <u>\$ 5,181</u> | <u>\$ 151</u> | <u>\$ 99,714</u> | <u>\$ 151,627</u> |

¹ See note 6 page A-18.

This schedule is prepared from the Statewide Budgeting & Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-15.

STATE AUDITOR'S OFFICE
SCHEDULE OF TOTAL EXPENDITURES, TRANSFERS OUT, & OTHER REDUCTIONS BY OBJECT BY PROGRAM
FOR THE FISCAL YEAR ENDED JUNE 30, 1995

| | Central Management | Insurance | Securities | Local Assistance Distributions ² | Federal Forest Reserve Funds ¹ | Pension Adj Retired Firemen ² | Fiscal Control And Management | Total |
|------------------------------------|-----------------------|---------------------|-------------------|---|--|--|-------------------------------------|----------------------|
| PROGRAM EXPENDITURES BY OBJECT | | | | | | | | |
| Personal Services | | | | | | | | |
| Salaries | \$ 210,692 | \$ 967,511 | \$ 268,407 | | | | \$ 293,881 | \$ 1,740,491 |
| Employee Benefits | 56,572 | 249,399 | 69,481 | | | | 85,875 | 461,327 |
| Personal Services-Other | | | | | | | 1,654 | 1,654 |
| Total | <u>267,264</u> | <u>1,216,910</u> | <u>337,888</u> | | | | <u>381,410</u> | <u>2,203,472</u> |
| Operating Expenses | | | | | | | | |
| Services | 14,713 | 118,734 | 15,955 | | | | 184,472 | 333,874 |
| Supplies & Materials | 12,507 | 136,761 | 17,568 | | | | 22,999 | 189,835 |
| Communications | 8,681 | 87,450 | 16,616 | | | | 337,335 | 450,082 |
| Travel | 1,920 | 34,142 | 2,865 | | | | (74) | 38,853 |
| Rent | 8,472 | 33,477 | 9,559 | | | | 13,770 | 65,278 |
| Repair & Maintenance | 1,121 | 3,742 | 2,982 | | | | 17,658 | 25,503 |
| Other Expenses | 1,978 | 19,045 | 2,840 | | | | 477 | 24,340 |
| Total | <u>49,392</u> | <u>433,351</u> | <u>68,385</u> | | | | <u>576,637</u> | <u>1,127,765</u> |
| Equipment and Intangible Assets | | | | | | | | |
| Equipment | 1,598 | 67,964 | 1,934 | | | | 9,857 | 81,353 |
| Total | <u>1,598</u> | <u>67,964</u> | <u>1,934</u> | | | | <u>9,857</u> | <u>81,353</u> |
| Local Assistance | | | | | | | | |
| From Federal Sources | | | | | \$ 14,631,717 | | | 14,631,717 |
| From Other Income Sources | | | | \$ 8,306,680 | | \$ 1,111,949 | | 9,418,629 |
| Total | | | | <u>8,306,680</u> | <u>14,631,717</u> | <u>1,111,949</u> | | <u>24,050,346</u> |
| Transfers | | | | | | | | |
| Accounting Entity Transfers | | | | | | | 211,976 | 211,976 |
| Total | | | | | | | <u>211,976</u> | <u>211,976</u> |
| Total Program Expenditures | <u>\$ 318,254</u> | <u>\$ 1,718,225</u> | <u>\$ 408,207</u> | <u>\$ 8,306,680</u> | <u>\$ 14,631,717</u> | <u>\$ 1,111,949</u> | <u>\$ 1,179,880</u> | <u>\$ 27,674,912</u> |
| PROGRAM EXPENDITURES BY FUND | | | | | | | | |
| General Fund | \$ 301,643 | \$ 1,198,171 | \$ 343,796 | | | | \$ 236,345 | \$ 2,079,955 |
| Special Revenue Fund | 16,468 | 520,054 | 64,411 | \$ 8,306,680 | \$ 14,631,717 | \$ 1,111,949 | 539,028 | 25,190,307 |
| Internal Service Fund | 143 | | | | | | 192,531 | 192,674 |
| Expendable Trust Fund | | | | | | | 211,976 | 211,976 |
| Total Program Expenditures | <u>318,254</u> | <u>1,718,225</u> | <u>408,207</u> | <u>8,306,680</u> | <u>14,631,717</u> | <u>1,111,949</u> | <u>1,179,880</u> | <u>27,674,912</u> |
| Less: Nonbudgeted Expenditures | | | | | | | 213,629 | 213,629 |
| Prior-Year Expenditure Adjustments | (319) | (4,401) | (1,891) | (307) | | | (331) | (7,249) |
| Budgeted Expenditures | <u>318,573</u> | <u>1,722,626</u> | <u>410,098</u> | <u>8,306,987</u> | <u>14,631,717</u> | <u>1,111,949</u> | <u>966,582</u> | <u>27,468,532</u> |
| Actual Budget Authority | 325,375 | 1,738,746 | 410,348 | 8,306,988 | 15,000,000 | 1,111,950 | 971,284 | 27,864,691 |
| Unspent Budget Authority | <u>\$ 6,802</u> | <u>\$ 16,120</u> | <u>\$ 250</u> | <u>\$ 1</u> | <u>\$ 368,283</u> | <u>\$ 1</u> | <u>\$ 4,702</u> | <u>\$ 396,159</u> |
| UNSPENT BUDGET AUTHORITY BY FUND | | | | | | | | |
| General Fund | | \$ 16,120 | \$ 249 | | | | \$ 89 | \$ 16,458 |
| Special Revenue Fund | | | 1 | \$ 1 | \$ 368,283 | \$ 1 | 1,227 | 369,513 |
| Internal Service Fund | \$ 6,802 | | | | | | 3,386 | 10,188 |
| Unspent Budget Authority | <u>\$ 6,802</u> | <u>\$ 16,120</u> | <u>\$ 250</u> | <u>\$ 1</u> | <u>\$ 368,283</u> | <u>\$ 1</u> | <u>\$ 4,702</u> | <u>\$ 396,159</u> |

¹ See note 7 on page A-19.

² See note 6 on page A-18.

This schedule is prepared from the Statewide Budgeting & Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-15.

Notes to the Financial Schedules

For the Two Fiscal Years Ended June 30, 1996

1. **Summary of Significant Accounting Policies**

Basis of Accounting

The office uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental, Expendable Trust and Agency Funds. In applying the modified accrual basis, the office records:

Revenues when it receives cash or when receipts are measurable and available to pay current period liabilities.

Expenditures for valid obligations when the department incurs the related liability and it is measurable.

State accounting policy also requires the office to record the cost of employees' annual leave and sick leave when used or paid.

The office uses accrual basis accounting for its Proprietary Fund. Under the accrual basis, as defined by state accounting policy, the office records revenues in the accounting period earned if measurable and records expenses in the period incurred, if measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the office received the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Basis of Presentation

The financial schedule format is in accordance with the policy of the Legislative Audit Committee. Effective July 1, 1996 the Legislative Audit Committee approved a new financial schedule presentation for agency audit reports. The new format includes nonbudgeted revenues and expenditures activity, as well as, all prior year adjustments for all financial schedules presented. In addition, financial activity for agency funds, if applicable to the agency, is included in the Schedule of Changes in Fund Balance and Property Held in Trust. The financial schedules included in this report are presented according to the revised format.

Notes to the Financial Schedules

The financial schedules are prepared from the Statewide Budgeting and Accounting System without adjustment except for agency funds which are adjusted to reflect the additions and reductions to property held in trust. Accounts are organized in funds according to state law. The office uses the following funds:

Governmental Funds

General Fund - to account for all financial resources except those required to be accounted for in another fund. The following divisions are funded in part by General Fund moneys: Central Administration, Insurance, Securities, and Fiscal Control and Management. The Fiscal Control & Management division included the Warrant Writer function in fiscal year 1994-95. Effective July 1, 1995, Warrant Writer moved to the Department of Administration.

Special Revenue Fund - to account for proceeds of specific revenue sources legally restricted to expenditures for specific purposes. Office Special Revenue Funds include certain Insurance and Securities Division activity. This includes the Firemen's and Municipal Police Officers' Pension Tax, Fire Prevention and Investigation Tax, Insurance Industry Continuing Education Program, and Securities Portfolio Registration Program. During fiscal year 1994-95, the office also recorded the receipt and disbursement of Federal Forest Reserve Funds to Montana counties in the Special Revenue Fund.

Proprietary Funds

Internal Service Fund - to account for providing goods or services to other agencies or departments on a cost-reimbursement basis. The office Internal Service Fund accounts for the cost of administering the Bad Debt Collections System, which was funded through a percentage of the bad debt collections made on behalf of state agencies. Effective July 1, 1995, the Bad Debt Collection System moved to the Department of Administration.

Fiduciary Funds

Trust and Agency Funds - to account for assets held by the state in a trustee capacity or as an agent for individuals, private organizations, other governments or other funds. Office fiduciary funds include Agency and Expendable Trust Funds.

Notes to the Financial Schedules

During fiscal year 1994-95, the Agency Fund accounted for the bad debt receipts and disbursements made on behalf of other agencies and general warrant functions. Effective July 1, 1995, both activities moved to the Department of Administration. In fiscal year 1995-96 the Agency Fund accounted for Federal Forest Reserve Fund activity. The Expendable Trust Fund accounts for state dated warrants. This function also transferred to the Department of Administration on July 1, 1995. The related accounting transactions were finalized by June 30, 1996.

2. Annual and Sick Leave

Employees at the office accumulate both annual and sick leave. The office pays employees for 100 percent of unused annual and 25 percent of unused sick leave credits upon termination. Accumulated unpaid liabilities for annual and sick leave are not reflected in accompanying financial schedules. In the Proprietary Funds, the increase in annual and 25 percent of the increase in sick leave are recognized as nonbudgeted expenses when the related liability is recorded at year end. The office absorbs expenditures for termination pay in its annual operational costs. At June 30, 1995 and at June 30, 1996, the office had a liability of \$200,468 and \$207,535, respectively.

3. Pension Plan

Employees are covered by the Montana Public Employees' Retirement System (PERS). The office's contribution to PERS was \$116,178 in fiscal year 1994-95 and \$105,641 in fiscal year 1995-96.

4. General Fund Balance

The General Fund is a statewide fund. Each agency does not have a separate General Fund since its only authority is to pay obligations from the statewide General Fund within their appropriation limits. Thus, on an agency's schedules, the General Fund beginning and ending fund balance will always be zero.

Notes to the Financial Schedules

5. **Reorganization**

The Warrant Writer and Bad Debt Collection Systems moved to the Department of Administration on July 1, 1995. The financial activity for these systems was recorded in the Fiscal Control and Management Program and was allocated among the General, Special Revenue, and Internal Service Funds.

In addition to the Warrant Writer and Bad Debt Collection Systems, the Department of Administration became responsible for certain related SBAS accounts. These include the general warrant, state dated warrant, and bad debt receipts and disbursements accounts. These accounts were previously recorded in the Agency and Expendable Trust Funds.

6. **Local Assistance Distributions**

In accordance with state law the office collects Fire Prevention & Investigation, Firemen's Pension, and Premium Taxes on insurance premiums written in the state of Montana. The Fire Prevention & Investigation Tax is distributed to cities and towns within Montana having a fire department relief association. The moneys are intended for the benefit and use of the association. The Firemen's Pension Tax is also distributed to cities and towns having fire department relief associations. This tax is used to finance pension payments made to retired firefighters. A portion of the Premium Tax is used to fund the Municipal Police Officers' Retirement System.

The above described distributions are recorded as Local Assistance Distributions on the Schedule of Total Expenditures by Object by Fund. The Firemen's Pension Tax distribution amounted to \$1,111,949 in fiscal year 1994-95 and \$1,050,286 in fiscal year 1995-96. The distribution for the Fire Prevention and Investigation Tax and the Municipal Police Officers' Retirement System totaled \$8,306,680 and \$8,895,849 in fiscal years 1994-95 and 1995-96, respectively.

Notes to the Financial Schedules

7. Federal Forest Reserve Funds

The office receives Federal Forest Reserve Funds from the U.S. Department of Agriculture. This revenue is derived from timber sales, grazing fees, land use fees, recreation charges, utility fees, mineral revenues, and admission and user fees related to National Forest land located in Montana. The office distributes these funds plus the related investment earnings to counties in accordance with the requirements of section 17-3-212, MCA. During fiscal year 1994-95, this activity was recorded in the Special Revenue Fund. Effective in fiscal year 1995-96, this activity is recorded in the Agency Fund. The distribution totaled \$14,631,717 and \$10,673,874 in fiscal years 1994-95 and 1995-96, respectively.

8. Agency Fund

The office uses the Agency Fund to account for assets held by the office in a trustee capacity for other state agencies or local governments. The types and amounts of activity accounted for in the Agency Fund are outlined below:

Additions to Property Held in Trust:

Fiscal Year 1994-95

| | |
|----------------------|--------------|
| Bad Debt Collections | \$ 3,184,612 |
|----------------------|--------------|

Fiscal Year 1995-96

| | |
|---|---------------------|
| Federal Forest Reserve Fund Receipts | 10,673,874 |
| Bad Debt Collections | 794 |
| Fraud Symposium Receipts | <u>3,925</u> |
| Total Additions to Property Held in Trust | <u>\$13,863,205</u> |

Reductions to Property Held in Trust:

Fiscal Year 1994-95

| | |
|------------------------|--------------|
| Bad Debt Disbursements | \$ 3,251,840 |
|------------------------|--------------|

Fiscal Year 1995-96

| | |
|--|---------------------|
| Federal Forest Reserve Fund Disbursements | 10,673,874 |
| Bad Debt Disbursements | 108,061 |
| Fraud Symposium Disbursements | <u>3,925</u> |
| Total Reductions to Property Held in Trust | <u>\$14,037,700</u> |

Agency Response

STATE AUDITOR
STATE OF MONTANA

Mark O'Keefe
STATE AUDITOR



COMMISSIONER OF INSURANCE
COMMISSIONER OF SECURITIES

October 30, 1996

OCT 31 1996

Mr. Scott A. Seacat
Legislative Auditor
Office of the Legislative Auditor
State Capitol
P.O. Box 201705
Helena, MT 59620-1705

Dear Mr. Seacat:

We have reviewed your financial compliance audit for the two fiscal years ended June 30, 1996. Our response to each audit recommendation follows:

Recommendation #1:

We recommend the State Auditor's Office develop appropriate methods to ensure the financial activities related to examinations of insurance and securities companies are properly recorded on the state's accounting records.

Agency Response:

We concur and will seek legislative authority for these expenditures.

Recommendation #2:

We recommend the State Auditor's Office develop formal procedures to ensure portfolio registration fee revenue is transferred to the General Fund in a timely manner.

Agency Response:

We concur. The State Auditor's Office will develop procedures to transfer these fees based upon a cash need basis. A schedule of transfers to the General Fund will be implemented.

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Mr. Scott A. Seacat
Page 2
October 30, 1996

Recommendation #3:

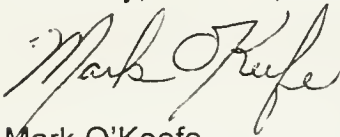
We recommend the State Auditor's Office seek legislation to clarify whether the Reinsurance Board is a state program or a nonprofit, nonstate entity.

Agency Response:

We concur. The State Auditor's Office will work with the Board of Montana Small Employer Health Carrier Reinsurance Program to seek legislation that will clarify whether the Reinsurance Program is a state program or a nonprofit, nonstate entity.

I would like to thank your staff for their time and effort during this audit. They were very helpful addressing issues that concerned my staff and pointing out areas that need improvement.

Sincerely,

A handwritten signature in cursive script, appearing to read "Mark O'Keefe".

Mark O'Keefe
State Auditor

MO/jhn

